Charting Your Course to Home Ownership

Applying for a Mortgage Loan

It is usually best to apply for a loan after you have a signed purchase agreement on the home you want to buy. However, it is possible to apply for "pre-approval" of a specified loan amount before then. This can be helpful when the buyer or seller is in a hurry to close the sale. But, since the pre-approval is generally good for only three months and the application fee is non-refundable, you could have to pay the fee again and repeat the process if the pre-approval expires before you buy a home.

Either way, when you have found the kind of mortgage you want with the best terms for your situation, it's time to make an appointment with the lender. You may want to request that a loan application be mailed to you and ask what you should bring with you to the interview.

The Loan Interview

It is important to prepare for the loan interview. Try to anticipate everything you will need and have all of the necessary information with you (including names, addresses with zip codes, phone numbers, dates of employment, etc.)

If you and a co-purchaser will both sign the mortgage, you should both go to the loan interview.

Loan Application Checklist

This checklist will help you prepare your loan application. It includes most of the information you will need to supply. However, some lenders have slightly different requirements, so check with your lender to ensure you collect all the required information.

Identification:

- Social Security number
- Driver's license or state-issued photo ID

Address History:

- Current address, name and address of landlord, and current monthly rent
- Previous address/landlord information if you've lived at current address for less than two years

Proof of Income:

- Employer information (names, addresses and phone numbers) for past two years

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- Recent pay stub showing year-to-date earnings
- Original W-2 forms for previous two (2) years
- Copies of tax returns for previous two years
- Proof of additional income (Social Security, interest income, alimony or child support, etc.)

Self-employed borrowers:

- Personal, partnership or corporation tax returns for the previous two years
- Current financial statements for the business

Assets:

- Recent statements for checking, savings, and brokerage accounts and CDs
- Statements for all retirement accounts (401(k), IRA, etc.) and non-retirement investments (stocks, bonds, mutual funds, etc.)
- Cash value of any life insurance policy
- Value of significant personal property, such as vehicles and boats that are paid in full

Liabilities:

- Statements (showing name of creditor, outstanding balance and monthly payment) for auto loans, student loans, credit cards, and other debts, including loans you have cosigned
- Alimony or child support you must pay

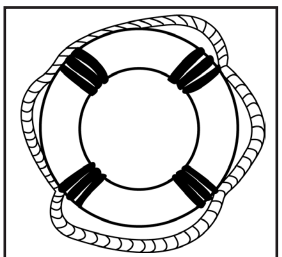
  NOTE: If you don't have an established credit history, provide the lender with canceled checks for rent, utilities and other financial obligations as proof of consistent payments.

Purchase Information:

- Copy of the home purchase contract
- Proof of your deposit
- A "gift letter" if the money for your down payment is a gift that doesn't have to be repaid

Payment:

- A check to cover the cost of the application, credit report, appraisal and other fees



Life Saver
Most loan decisions are made with an Automated Underwriting System (AUS), rather than a simple qualifying ratio.

Qualification

If you have not already been prequalified by this lender, the loan officer will first want to make sure you qualify for the loan you are applying for. Be sure to ask the lender about loan requirements and restrictions if you are eligible for any of the special affordable loan programs with flexible qualifying guidelines.

The Loan Application

If you have not already done so, the lender can help you fill out the loan application. This form is designed to provide the information the lender needs to evaluate the risk involved in lending money to you (the likelihood that you will or won't repay the loan). You will not help yourself by trying to cover up past credit problems in hopes that the lender won't discover them. Be completely truthful, but don't try to show why past problems are behind you.

Once you have signed the loan application, you may be bound to accept the loan if it's offered or to pay the lender's processing costs if your application is rejected. Be sure the application states amounts and terms that are acceptable to you. Don't sign if you are unsure about ANYTHING. When in doubt, check it out.

At this time, you may be required to pay an application fee, which should cover the cost of the appraisal and credit report only.

Locking in the Current Rate

If you think interest rates might rise during the time the loan is being processed, the lender may agree to lock in the current rate (and number of points) for a certain period. Find out when the lock-in takes effect and how long it remains in effect, and get the lock-in agreement in writing. A lock-in for a very short period may be useless; you want something that will get you to closing without having to be extended.

Estimates of Closing Costs

Within three days after you have applied for a home loan, the lender is required to give you an itemized estimate of the costs to settle (or close) the loan. This report is referred to as a "good faith estimate." The lender must also give you a copy of the government publication, *A Home Buyer's Guide to Settlement Costs*. Read it!

Items included in the good faith estimate document:

- **Appraisal** –The lender will arrange to have the property appraised, a service for which you will probably be charged as part of the loan application fee. The lender's professional appraiser will determine the market value of the home. This is important because the loan amount cannot be larger than a given percentage of the value of the property. The amount of mortgage insurance you need to buy (if any) is also based on the market value of the home.

  If the appraised value is less than the purchase price, the amount of your mortgage may be smaller than you had planned, and you could have to come up with a larger down payment. On the other hand, if you have included an appraisal contingency in your contract, you can renegotiate the purchase price or back out of the deal if the appraisal is low.
- **Loan Application Origination** or **Processing Fee** – This charge covers the expenses of preparing mortgage documents, legal service, borrower credit investigation, notary charges, appraisal fee and any other fees.
- **Title Search and Title Insurance** – Title Insurance is usually paid by the seller because he or she guarantees the title to be good. The buyer usually pays for the mortgagee title policy. This protects the lender against unrecorded title defects.
- **Abstract of Title** – Summary of all recorded documents affecting a particular piece of real estate to document a clear and marketable title.
- **Survey** – The survey determines the precise legal boundary lines of a property, location of improvements, easements, right of ways, encroachments and other physical features. Sometimes, the seller may incur this expense if he or she is requested to do so.

- **Deed Recording Fee** – Charged by parish clerk of court's office to legally record your deed.
- **Attorney's Fee** – This fee is charged by the attorney for legal advice during the various stages of buying.
- **Unpaid Special Assessments** – Any assessment for streets, sidewalks, sewers, etc. that are levied or pending against the property before closing usually must be paid if mortgage financing is obtained.
- **(Discount) Points** – A point is one percent of the mortgage value. Thus, the borrower who must pay one point on a $100,000 mortgage would pay $1000, up front. Discount points are interest paid up front. They can be negotiable depending on the loan product.
- **Prepaid Property Taxes** – At the time of closing, the lender will often require the buyer to deposit one to six months' property taxes in an escrow account.

Truth in Lending

Your lender is also required to give you a Truth In Lending document, which fully discloses all the terms and conditions of the loan. Some of the terms required to be disclosed include:

- Rate of Interest – This is the largest single determinant of the cost of your loan. Be watchful, a lender could promise a lower-than-market interest rate because the difference may be made up through other financing charges.
- Annual Percentage Rate (APR) – The APR is the cost of your loan expressed as a yearly percentage rate, such as 5 percent or 6 percent. In the Truth In Lending disclosure you will notice the APR may differ from what your loan officer disclosed to you. This is because the APR includes all fees and costs associated with the loan.

It is normal to see a slight difference between the interest rate and the APR because of the normal costs of the loan. Some lenders may take advantage of people by offering a competitive interest rate and adding extra fees after the normal costs of a loan. This increases the disclosed APR of the loan. **If the APR is extremely different from the original quoted interest rate, do not be afraid to question this.**

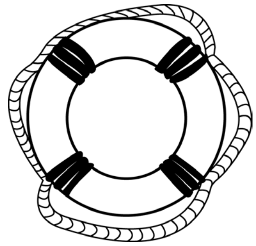
Speeding the Approval Process

Be sure to act quickly in the lender's request for information while your loan is being processed. It's also a good idea to call the lender now and then to check on the status of your application. You can then contact your employer or others who must provide documents or other information to the lender before your loan can be approved.

Loan Processing

In processing your loan application, the lender will mainly be interested in two things:

- the property you plan to buy (since it is collateral for the loan), and
- your financial situation and your credit history (since they will show your ability and your commitment to repay the loan).



Life Saver
Save money by cancelling mortgage insurance (PMI) when you have accrued equity equal to 20% of the amount of your mortgage.)

To get information about these, the lender will arrange for an appraisal of the property, request credit reports on you and any co-borrowers, and verify the information in your loan application.

Credit Report

The lender also will order a credit report on you, your spouse and any other co-purchasers. The charge for this is usually included in your application fee. The credit bureau's report will show how you have handled past debt and credit accounts, such as car loans, charge accounts with stores, credit cards and any other purchases made on credit. If you have already seen your credit profile; there will be no surprises.

When there is little or nothing on your credit report, you may be able to establish a nontraditional credit history by providing evidence that shows you are a dependable credit risk. Ask your lender for suggestions of what types of evidence you could provide to show your credit worthiness.

It is unusual for the lender to ask for a written explanation of any problems that appear on your credit report (although it is best to clear them up before applying for your mortgage). Even one late payment on just one account usually requires an explanation. Don't be alarmed by this request. Just respond promptly with a truthful statement about whatever caused the late payment(s).

Lenders are also likely to order your credit score. This tool helps lenders decide whether to offer you credit and at what term, such as interest rate and loan size.

Verifications

The lender will also verify (check to confirm) the information on your loan application about your income and employment history, your assets (checking and savings accounts, etc.) and your rent payment history.

Approval of Mortgage Insurer

If your down payment will total less than 20% of the appraised value of the home you want to buy, you will probably need to purchase mortgage insurance. In general, the borrower pays a mortgage insurance premium to buy insurance that protects the lender in case the borrower defaults. Mortgage insurance can make it possible for you to make a down payment of only 5% (sometimes less in special programs).

If mortgage insurance is needed, the loan will also have to be approved by the mortgage insurer. If you are obtaining an FHA, VA or USDA Rural Development loan, the loan and property must also meet FHA, VA or USDA Rural Development standards and restrictions.

Commitment Letter

When your loan is approved, the lender will **send you a commitment letter**. This is the formal loan offer. It will **state the loan amount** (purchase price minus down payment), **the term** (number of years you have to repay the loan), the loan **origination fee** (a percentage of the loan amount), the points (up front finance charge), the annual percentage rate or **APR** (the actual finance charge taking into account the interest rate, origination fees, points and mortgage insurance fees) and the **monthly charges** (principal and interest, property taxes and insurance or PITI).

You will be given a set amount of time to accept the loan offer and to close the loan. Go over the commitment letter before you sign it. Be certain you understand and will be able to meet any conditions set by the lender. By signing the commitment letter, you accept the terms and conditions of the loan offer.

Loan Denial

If your loan application is not approved, find out why. You may be able to correct the situations that led to the denial or try to find a lender with different or flexible approval requirements. One rejection does not mean all lenders will reject your loan application. Lenders are required to explain in writing a decision to deny credit. Go back and talk with the loan officer to find out details about the reasons. Some reasons may be corrected quickly (such as renegotiating the price on a home with a low appraisal), but others may require long-term solutions (such as a poor credit history).

You then have at least four options: work to correct the problem, apply for a different mortgage, appeal the decision or postpone buying a home until your situation has improved. Here are some common reasons for loan denial and ideas to consider when planning your course of action:

Low appraisal

- Renegotiate the purchase price with the seller.
- Ask the seller to correct problems which affected the appraisal or set up an escrow account to pay for repairs after the sale.
- Buy a different home.

Not enough income

- Find or wait for a loan with a lower interest rate (such as an ARM or bond-issue loan).
- Find an affordable loan program with flexible qualifying guidelines.
- Choose a less expensive home to buy.
- Get a co-signer.
- Think about ways your family can increase your household income.
- Reapply later when your income is higher.

Unstable income

- Ask your employer to send a letter verifying that your income will be stable in the future (if that is the case).
- Seek a stable source of income for someone in your household.

Too much debt

- Work out a repayment plan, and send the lender a letter explaining your debt reduction plan.
- Choose a less expensive home to buy.
- Find an affordable loan program with flexible qualifying guidelines or lower interest rate.

- Get a co-signer.
- Reapply later after you have reduced your debt.

Problems on credit report

- Get a free copy of your credit report from http://.www.annualcreditreport.com
- Check it for accuracy; challenge and correct any errors you find.
- Ask the credit bureau to add to your file your written explanation of any unresolved disputes.
- Send a brief statement to the bureau to explain late payments caused by loss of job or medical bills.
- Contact your creditors, set up a repayment plan and make whatever size payments you can to show good faith.
- Contact a nonprofit credit counseling service.
- Seek family financial management information and education from your parish extension office of the LSU AgCenter.

Not enough saving for down payment and closing costs

- Ask relatives to help.
- Buy private mortgage insurance.
- Look into FHA, VA, USDA Rural Development and other affordable loan programs which require little or no down payment.
- Seek a lease-purchase arrangement (rent with option to buy).
- Postpone buying a home, and develop a budget and savings plan to reach your financial requirements.

Disqualified property (Government-assisted loan programs may have property standards or restrictions for homes financed.)

- Choose a different home to buy.
- Find a loan program that does not have property restrictions.
- Negotiate with the seller to bring the property up to standards.

Adapted from: Reichel, C. (1998). Your Path to Home Ownership. Baton Rouge, La.; LSU AgCenter.

Additional References:
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LSU AgCenter Writing Team:
Jeanette A. Tucker, Ph.D., Professor
Deborah L Hurlbert, Extension Associate
Sheri Richard Fair, Extension Agent, Ascension Parish
Deborah C. Cross, Extension Agent, Iberville Parish
Cynthia C. Richard, Extension Agent, Calcasieu Parish
Cynthia B. Stephens, Extension Agent, Ouachita Parish

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Louisiana State University Agricultural Center
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Louisiana Cooperative Extension Service
Paul D. Coreil, Vice Chancellor and Director
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